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HOUSE BILL 1406

By Boyer

AN ACT to amend Tennessee Code Annotated,
Title 67, Chapters 1 and 4, relative to
tax refunds and to franchise, excise
taxes.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF TENNESSEE:

SECTION 1. Tennessee Code Annotated, Section 67-4-2004 is amended by deleting subsections (27) and (28) in their entirety.

SECTION 2. Tennessee Code Annotated, Section 67-4-2006(b)(1)(F) is amended by inserting the words "franchise or" between the word "the" and the word "excise".

SECTION 3. Tennessee Code Annotated, Section 67-4-2006(b)(1) is amended by deleting subitems (I) and (J) in their entirety and substituting instead the following:

(I) Any net loss and any item of expense or loss that meets all of the following criteria:

(i) is included in the determination of the taxpayer's net earnings or loss;

(ii) is from an S-corporation, an entity treated as a partnership for federal tax purposes, or a single member limited liability company that is subject to and files a return for the tax imposed by this part; and

(iii) is allocated to a partner or shareholder of such entity referred to in subitem (ii).

SECTION 4. Tennessee Code Annotated, Section 67-4-2006(b)(2) is amended by deleting subitems (K) and (L) in their entirety and substituting instead the following:

(K) Any net gain and any item of income that meets all of the following criteria:

(i) is included in the determination of the taxpayer's net earnings or loss;

(ii) is from an S-corporation, an entity treated as a partnership for federal tax purposes, or a single member limited liability company that is subject to and files a return for the tax imposed by this part; and

(iii) is allocated to a partner or shareholder of such entity referred to in subitem (ii).

SECTION 5. Tennessee Code Annotated, Section 67-4-2007 is amended by deleting subsections (d) and (e) in their entirety and substituting instead the following:

(d) (1) For purposes of the excise tax levied by this part, a business entity shall be classified as a corporation, partnership, or other type business entity, consistent with the way the entity is classified for federal income tax purposes, and subject to tax in accordance with this Part 20. Entities that are disregarded for federal income tax purposes, except for limited liability companies whose single member is a corporation, shall not be disregarded for Tennessee excise tax purposes.

(2) This subdivision applies to qualified subchapter S subsidiaries with an election in effect under Section 1361(b)(3)(B)(ii) of the Internal Revenue Code, qualified real estate investment trust subsidiaries described in Section 856(i) of such Code, and partnerships or other entities, to the extent they are owned directly or indirectly by a real estate investment trust. Notwithstanding any provision of law to the contrary, any such entity, to the extent it is disregarded for federal income tax purposes and included in the

federal return filed by its owner, shall be included in the owner's excise tax return as a division of the owner.

(3) In the event that a corporation, partnership or other entity is only partly owned, directly or indirectly, by a real estate investment trust, such entity shall be considered a separate entity from its owners for purposes of the tax imposed by this part, but only to the extent that it is directly or indirectly owned by entities that are not real estate investment trusts. Such an entity shall file an excise tax return and shall compute its net earnings (losses) for excise tax purposes on all its business operations; provided that the excise tax base shall be computed by multiplying the net earnings (losses) so computed by the percentage of ownership by entities or individuals that are not real estate investment trusts.

(e) Except for unitary groups of financial institutions, business entities described in subsection (d)(2) above, business entities required or permitted by law to file excise tax returns on a combined or consolidated basis, and business entities upon whom a variance to the contrary has been imposed or granted under Section 67-4-2014, each taxpayer shall be considered a separate and single business entity for Tennessee excise tax purposes and shall file its Tennessee excise tax return on a separate entity basis reflecting only its own business activities even though it may have been disregarded for federal purposes or filed a consolidated federal income tax return with other members of its business group. The federal taxable income computed on a separate entity basis excise tax return and subject to adjustments set forth in Section 67-4-2006 shall be the same federal taxable income that would have been computed on the taxpayer's federal return if it had been filed on a separate entity basis rather than disregarded or filed on a consolidated basis.

SECTION 6. Tennessee Code Annotated, Section 67-4-2008(a) is amended by deleting subdivision (10) in its entirety and substituting instead the following:

(10) (A) Any family-owned non-corporate entity, at least sixty-six and sixty-seven hundredths percent (66.67%) of whose income is passive investment income.

(B) For purposes of this subdivision (10):

(i) "Family-owned" means that at least ninety-five percent (95%) of the entity is owned by:

(a) one individual person; or

(b) individuals who are lineal descendants of at least one common grandparent; or

(c) the spouse or former spouse of individuals described in subdivision (10)(B)(i)(a) and (b) above; or

(d) the estate of a deceased individual who, while living, was an owner as described in subdivision (10)(B)(i)(a) through (c) above; or

(e) one or more trusts, if all the beneficiaries and owners of such trusts are related as described in subdivision (B)(i) (a) through (d) above.

(f) one or more trusts described in section 4947(a)(2) of the Internal Revenue Code of which all the non-charitable beneficiaries are individuals or trusts described in subdivision (B)(i) (a) through (e) above.

(ii) A legally adopted child of an individual shall be treated as the child of such individual by blood.

(iii) "Passive investment income" means gross receipts attributable to interest, dividends, annuities, royalties, net income from publicly traded partnerships, income (including dividends) from real estate investment trusts, and gains from the sale or exchange of property that produces, or that is capable of producing, passive investment income; provided, however, that gross receipts do not qualify as passive investment income if, at any time during the tax year, any owner or beneficiary of the family-owned non-corporate entity participates in the

day-to-day management or operation of the underlying activity that generates such gross receipts.

SECTION 7. Tennessee Code Annotated, Section 67-4-2012 is amended by deleting subsection (k) in its entirety.

SECTION 8. Tennessee Code Annotated, Section 67-4-2105 is amended by adding the following language after the last sentence of subsection (a):

In the event that an exempt entity cannot determine the portion of its net worth or real or tangible personal property attributable to activities unrelated to and outside the scope of the activities that gave the entity its exempt status, the dollar amount of such property and net worth shall be determined by applying a ratio, the numerator of which shall be non-exempt gross receipts as determined for federal income tax purposes and the denominator of which shall be total gross receipts from all sources.

SECTION 9. Tennessee Code Annotated, Section 67-4-2105, subsection (a), is amended by deleting the words and punctuation “or under the provisions of subsection (b)” immediately after the symbol, numbers and punctuation “§ 67-4-2008”.

SECTION 10. Tennessee Code Annotated, Section 67-4-2105 is amended by deleting subsection (b) in its entirety and relettering the remaining subsections accordingly.

SECTION 11. Tennessee Code Annotated, Section 67-4-2106 is amended by deleting subsection (c) in its entirety and substituting instead the following:

(c) (1) For purposes of the franchise tax levied by this part, a business entity shall be classified as a corporation, partnership, or other type business entity, consistent with the way the entity is classified for federal income tax purposes, and subject to tax in accordance with this Part 21. Entities that are disregarded for federal income tax purposes, except for limited liability companies whose single member is a corporation, shall not be disregarded for Tennessee franchise tax purposes.

(2) This subdivision applies to qualified subchapter S subsidiaries with an election in effect under Section 1361(b)(3)(B)(ii) of the Internal Revenue Code, qualified real estate investment trust subsidiaries described in Section 856(i) of such Code, and partnerships or other entities, to the extent they are owned directly or indirectly by a real estate investment trust. Notwithstanding any provision of law to the contrary, any such entity, to the extent it is disregarded for federal income tax purposes and included in the federal return filed by its owner, shall be included in the owner's franchise tax return as a division of the owner.

(3) In the event that a corporation, partnership or other entity is only partly owned, directly or indirectly, by a real estate investment trust, such entity shall be considered a separate entity from its owners for purposes of the tax imposed by this part, but only to the extent that it is directly or indirectly owned by entities that are not real estate investment trusts. Such an entity shall file a franchise tax return and shall compute its net worth for franchise tax purposes on all its business operations; provided that the franchise tax base shall be computed by multiplying the net worth so computed by the percentage of ownership by entities or individuals that are not real estate investment trusts.

(4) Except for unitary groups of financial institutions, business entities described in subsection (c)(2) above, business entities required or permitted by law to file franchise tax returns on a combined or consolidated basis, and business entities upon whom a variance to the contrary has been imposed or granted under Section 67-4-2112, each taxpayer shall be considered a separate and single business entity for Tennessee franchise tax purposes and shall file its Tennessee franchise tax return on a separate entity basis reflecting only its own business activities even though it may have been disregarded for federal purposes or filed a consolidated federal income tax return with other members of its business group.

SECTION 12. Tennessee Code Annotated, Section 67-4-2108 is amended by deleting the second sentence of subsection (a)(1) in its entirety and substituting instead the following language:

Notwithstanding the foregoing, the sole franchise tax measure of a business entity that elects to be treated as a real estate investment trust under Section 856 of the Internal Revenue Code shall be net worth computed in accordance with the provisions of Section 67-4-2106.

SECTION 13. Tennessee Code Annotated, Section 67-4-2108(a)(3) is amended by deleting the words, "For this purpose" at the beginning of the next to last sentence thereof and substituting instead the words "For purposes of this section".

SECTION 14. Tennessee Code Annotated, Section 67-4-2111 is amended by deleting subsection (k) in its entirety.

SECTION 15. Tennessee Code Annotated, Section 67-1-1802(a) is amended by deleting the fifth (5th) sentence of subdivision (1) and substituting instead the following language:

The authority granted in this subdivision extends only to taxes for which a claim is filed, with the commissioner under oath and supported by proper proof, within three (3) years from December 31, of the year in which the payment was made; provided, however, that a franchise, excise tax refund shall not be made unless the refund claim is filed within one (1) year from December 31 of the year in which payment was made.

SECTION 16. Tennessee Code Annotated, Section 67-1-1802(a) is amended by deleting the language in subdivision (2) in its entirety and substituting instead the following:

The commissioner is authorized to make refunds, within three years from December 31 of the year in which the payment was made, without a claim being filed, if the commissioner is in possession of proper proof and facts that a refund is due;

provided, however, that no refund for franchise or excise taxes shall be made after one year from December 31 of the year in which payment was made.

SECTION 17. This Act shall take effect upon becoming law, and shall apply to tax years beginning on or after January 1, 2001, the public welfare requiring it.